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Report of the Committee on Valuation of the...

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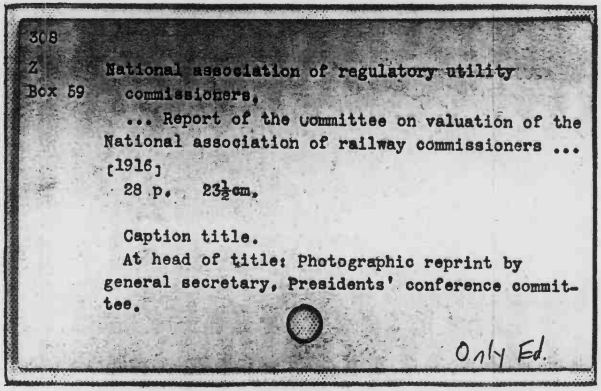
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of the

REPORT OF THE COMMITTEE ON VALUATION
of the
NATIONAL ASSOCIATION OF RAILWAY COMMISSIONERS

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Scope of the Committee's Jurisdiction.

When the Association met in convention in San Francisco in 1915, two committees had to do with the subject of railroad valuations; a standing committee on "Railroad Taxes, and Plans for Ascertaining Fair Valuation of Railroad Property," and a Physical Valuation Committee, which had to do with the special problems growing out of the federal appraisal of common carrier properties under the Valuation Act of March 1, 1913. At the San Francisco convention the Association recognized that the duties and work of its members had been extended by the process of transforming railroad commissions into public service commissions. Therefore the two valuation committees were in effect consolidated, and the present general committee on Valuation provided for, with duties relating both to railroads and public utilities. Ever since the present committee was named the federal appraisal has been in the critical formative stage, and therefore the work of the Committee has been entirely directed to the subject matter of the valuation of the property of the interstate carriers being made by the Interstate Commerce Commission.

The interest of the State Commissions in the Appraisal.

For many years this Association urged Congress to undertake the appraisal of the railroads of the nation. Such an appraisal has been provided for under Congressional authority, and is now being made. At every convention of the Association since the appraisal began a sentiment has been strongly voiced for a more active participation by the state commissions in the valuation than there could be if they waited passively until the principal part of the work had been done. This sentiment grew out of a conviction as to the nature of the underlying duty of the state commissions, and an insight into the possibilities for evil which a perfunctory or ex parte appraisal might bring upon the states separately and as a collective national unit, based upon an experience in local railroad valuations which indicated that there was an imperative necessity for active representation on behalf of the public. Whether the duty of the state commissions is statutory or not, there is a practical and necessary call for them to interest themselves earnestly in the federal appraisal to perform the full service to their commonwealths which their constituents have the right to demand. This Association has taken it as self-evident that many important questions, with grave results and enormous sums involved, will go before the federal Commission without full statement of the claims of the general public interest unless the state commissions are heard. A number of these questions of fundamental principles have already been fully argued before the Commission by the members of this Committee and its representatives. This assumption is based on no spirit of hostility to the carriers, and manifests no distrust of the industry, high ideals, and intelligence of the Inter-

state Commerce Commission or its employees. The state commissions have nothing to ask but that the facts be found, the whole facts, and nothing but the facts, and believe that nothing can be taken as an established fact which will not be strengthened as a finding if it first be successfully maintained as against critical analysis from opposing points of view. This analysis, if it is to be constructive, must be made while the work progresses, and before the results are in fixed form.

Basis for the interest of the States and the State Commissions.

It is unnecessary to recapitulate the reasons which have been well stated at previous conventions of this Association on many occasions. The consensus of opinion is that in ultimate and legal effect, if not in nominal and immediate result, the federal valuation will be the touchstone whereby to test the lawfulness of all railroad rate systems, state or interstate. The states will be bound directly as to the whole fabric of interstate rates by which the state's commerce is governed, and will be bound indirectly as to the whole interwoven intrastate rate structure through the application of constitutional principles which have recently become familiar. The findings doubtless will be controlling in issues which are entirely beyond the present scope of the proceedings, and which cannot now be foreseen. The possible event of governmental acquisition of the instrumentalities of commerce suggests itself. It will be difficult for the commission of any state to convince its own constituents that the appraisal—made after the expenditure of millions of money and years of time, with all the authority of the national government behind it, after notice to the state and hearing of its objections—is wrong and the local commission holding different opinions is right.

That there will be a marked effect upon public service corporation finance goes without saying. Already certain of the carriers have evinced great timidity lest the tentative findings of valuation made by the Commission should become public property and should be "misunderstood" by the investing public, whereby the credit of the carriers should be needlessly impaired. On the other hand, a saturnalia in the market would follow the adoption of some of the claims of the carriers, and no one could object that the proceedings were not even in good taste.

When the principles applicable are determined they will largely control analogous cases with respect to other public utilities than those within the scope of the Act to Regulate Commerce, with which the state commissions have everything to do. The state commissions may therefore find too late that the valuation principles are effectually settled for them in all matters which relate to purely state commerce, and without their being heard except as they voice their views in the present proceedings.

Instructions Given the Valuation Committee.

The San Francisco convention took definite action for the continual representation of the states at Washington during the appraisal, but only after the subject had been brought before the Association and its various committees year after year, and the necessity had been so clearly shown that the vote was unanimous as to what should be done. Representation during the appraisal was so strongly deemed advisable at a conference held at Chicago in May, 1915, participated in by twelve state commissions, that by unanimous action a committee was appointed to consider the matter further, to arrange for funds, etc. A conference at Washington held later in the same month, having to do directly with the federal valuation, deepened the sentiment; and the fifteen states participating were again unanimous as to the necessity for representatives of the states being continually in touch with the situation at Washington, in order that the states might at all times be informed, and that their interests might be safeguarded. The extremely thorough organization developed by the carriers served to emphasize the need. The special committee of five reporting to the last convention of this Association on the federal appraisal most strongly urged this course, and stated that its recommendation was unanimously approved by the Executive Committee of the Association. A special committee of ten (nine of whom acted in the investigation) canvassed the situation carefully during the San Francisco convention, and its unanimous report was in favor of the establishment of representation in Washington. The proposition was then long and carefully debated before the convention, and as the result, the Association unanimously adopted the following resolution:

> "That the several states should be represented by counsel at the hearings to be held before the Interstate Commerce Commission on questions relating to the valuation of railroads, and that the Committee on Valuation should be authorized to secure funds, employ counsel and other employees, if necessary, and to do any and all things which will enable the states to assist the Interstate Commerce Commission in reaching a fair and just conclusion in this most important matter. The counsel to be selected by the Valuation Committee shall be free to take such position on issues before the Commission as shall to him seem wise and just. No position taken by said counsel shall be interpreted or used as an estoppel on any member of this organization from taking such position as shall be deemed right by such member in any court or commission, state or federal, at this time or any future time. Each commission retains full authority to be represented in any and all hearings relative to the national appraisal, as it may desire, and to take any position on any issue which may seem right to said Commission."

About twenty states showed their earnestness of purpose by making definite pledges running for two years for the support of the work the Committee was directed to undertake: other states have since the convention made similar pledges; and others have expressed their good will and tendered their support.

Steps Taken by the Committee in the Carrying Out of the Association's Instructions.

This Committee has obeyed the instructions given it by the deliberate and unanimous determination of the Association. It has been taken as settled that in the judgment of the state commissions they "have as vital an interest in the valuations now being made as the federal commission," (Report of Physical Valuation Committee, 1915 convention, proceedings, p. 385). The Committee has taken its grant of power as a mandate that the authority conferred should be exercised with vigor and a serious purpose; and to that end the members of this Committee have given their best thought and efforts. As will appear later in this report, they have held sessions aggregating several weeks of time, have participated in hearings before the Commission and the Division of Valuation, and have prepared briefs and arguments when the public interest required, and have employed counsel and now maintain representation in Washington for the purposes specified in the Association's instructions, to render assistance to the Interstate Commerce Commission and to the states, and to see that the rights of the states are safeguarded. The Committee's plans and expectations have been curtailed for financial reasons; and the Committee realizes fully there is opportunity for a greater service than it has been able to perform. Yet the Committee is convinced that the progress already made has fully justified the course the Association has followed.

Unpreparedness of Many State Commissions.

Many state commissions, earnestly desirous of safeguarding the interests of their states, now find themselves without either the experience or the administrative machinery necessary to enable them to cope with the situation presented by the appraisals as they reach completion. In practice such commissions are excluded from effective participation in the appraisal, both by the brevity of the time for protest allowed by law and by the prohibitive expense and practical impossibility of organizing a corps of experts upon such short notice. These states must perforce practically let their interests in the federal appraisal go by default, except for such assistance as may be rendered in a spirit of comity by sister states acting through this Committee. The federal appraisal ought not to be permitted to go by default by any state; and the Committee, recognizing that fact, has tendered its good offices to every state commission in which valuations have been matured, and has rendered and will render all possible assistance to such state commissions as may desire or will receive it, in the way of advice as to matters of general policy or specific facts or principles. This tender is made to all the states alike, whether contributors to the support of the Committee or not. It is gratifying to be able to report that a spirit of cooperation has generally been found to exist;

and the fostering of this spirit and the putting of it into practical effect this Committee conceives to be one of its chief duties.

Hearings before the Commission.

When the present Committee was appointed, an extended hearing had already been held before the Commission on certain of the fundamental principles involved in the valuation proceedings, in which the carriers had been strongly represented and had filed a full and able written argument. Upon its appointment this Committee sought and obtained from the Commission the opportunity to be heard orally upon these fundamental questions, with leave for the states to file briefs. A preliminary conference of members of the Committee was held and preparations were made for the presentation of the issue from the standpoint of the states. A brief was prepared and filed by the Committee (credit for which is chiefly due to Commissioner Henshaw, of Oklahoma), and in addition, the commissions of the states of California, Kansas, Minnesota, and Oregon—all of which were represented on the Committee—filed briefs in their own behalf. On January 26 to 28, inclusive, oral arguments were held before the full Commission, upon the fundamentals in the appraisal. Arguments were made by members of the Committee, and by Hon. A. E. Helm, Commerce Counsel of the Kansas Commission, upon the following topics, generally stated:

Mr. Thelen: The construction of the Valuation Act, particularly with reference to the ascertainment of an ultimate sum as representing *the* value of the property; aids, gifts, grants and donations; and intangible values.

Mr. Helm: Ascertainment of original cost to date; and principles governing land values.

Mr. Niles: Meaning of the requirement for ascertainment of the cost of reproduction less depreciation.

Mr. Aitchison: Importance of ascertaining and stating investment in operating property constructed out of surplus earnings, depreciation reserves, etc.

Mr. Shaw: Treatment of solidification and adaptation in ascertainment of grading quantities.

Mr. Bristow: Construction of the Valuation Act, as to ascertainment of a final value.

Mr. Elmquist: Purpose of the Valuation Act; property to be included; and a rational and reasonable theory of reproduction new.

The argument was concluded, after answer by the carriers, by Mr. Thelen.

Copies of the various briefs filed and of the transcript of the proceedings before the Commission upon the oral argument were sent the various state commissions at the time, and further comment may be omitted.

The Committee has twice since the January hearing participated in conferences of a rather formal nature before the Division of

Valuation. On May 26 the Division of Valuation submitted for consideration and criticism the reports of its Accounting, Engineering and Land Sections upon the properties of the Texas Midland Railroad. At this conference representatives of the Texas Commission appeared in its behalf and Mr. Aitchison appeared as Solicitor for the Valuation Committee. On June 19 to 22, inclusive, conferences were held as to the reports of the various Sections of the Division of Valuation upon the Atlanta, Birmingham & Atlantic. the Norfolk Southern, and the Kansas City Southern systems. These conferences were participated in by representatives of the states of Virginia and Kansas, and by all members of the Valuation Committee who could attend. The importance of a full discussion of the results of the policy of the Division of Valuation as applied in these first cases is immediately apparent. As the carriers were strongly and numerously represented the frank, full, and somewhat informal discussion between their representatives, the state commissions, and the Division of Valuation at least developed the issues and demonstrated their importance.

Establishment of Bureau at Washington.

It was the unanimous conclusion of the Committee, after the argument before the Commission in January, that it was unwise further to delay arranging for a continuous representation on behalf of the states at Washington during the appraisal. The subject was thoroughly canvassed; and in reaching this conclusion, the committee was aided by the advice of a number of other members of the Association who were in attendance upon the argument. The proposition had the hearty encouragement of the Chairman of the Interstate Commerce Commission itself, and of the Director and members of the Advisory Board of the Division of Valuation. This Committee, therefore, deemed it to be its plain duty to provide such representation. The remaining members of the Committee decided to ask Mr. Aitchison, Chairman of the Oregon Commission, to leave his work in that state and to become the solicitor for the Committee and its Washington representative. The Committee's call was respected, and Mr. Aitchison retired from the Oregon Commission, and, since the establishment of the Washington bureau early in May, 1916, has devoted his entire time to the service of the state commissions in connection with federal valuation matters.

It happened that practically at the same time the Committee's representation was established at Washington, the Division of Valuation completed its work in the first series of valuations undertaken by it. Copies of the engineering, land and accounting reports (as far as they were completed) were transmitted to the interested state commissions and to the carriers, and made available to the Valuation Committee. Conferences were called before the Director and Members of the Advisory and Engineering Boards, with respect to the reports, as has already been stated. As careful

analyses were made of the reports as time would permit, and a number of conferences have been held between the Solicitor of the Committee and representatives of the state commissions interested, both in Washington and elsewhere. The Committee through its Solicitor has taken the lead in getting interested state commissions into conference, for the purpose of careful analysis of the valuation situation. A number of properties have been inspected with the state commissions and their engineers. Typical field notes prepared by the federal engineers have been checked and field parties visited to obtain first hand information as to the manner in which the work is being done. There have been daily discussions with officers or employees of the Commission concerning features of the work which affected the states, either in respect to matters of policy in respect to the appraisal, or as to administrative features of the undertaking calculated to make the work of the federal authorities more accessible and useful to the state commissions for their own particular and local purposes. A number of special studies have been undertaken as to various important subjects of general application, and a large amount of unit cost data has been assembled, supplied by the engineering departments of various commissions, which the Committee hopes to be able to amplify and coordinate, and then make available for the general use of the state commissions. The Washington Bureau has at all times kept each member of the Valuation Committee fully advised as to the status of the work and the various problems which have come up, and there has been full and free interchange of ideas so that the work of the Bureau and the wishes of the Committee have been entirely in harmony. Progress reports have been sent to the state commissions from time to time and special information supplied to the state commissions interested in special valuations under way or reaching completion.

Finances.

The Committee has received financial support from the Commissions of the following states: Iowa,
California, Florida, Illinois, Kansas, Kentucky, Maine, Massachusetts, Minnesota, Nebraska, New Hampshire, New York (First District), Oklahoma, Oregon, Virginia, and West Virginia.

A number of other commissions expressed a desire to contribute to the support of the work of the Committee, but found that their local appropriation acts prevented them from aiding in the support of the Committee. Several commissions which found themselves in this position have indicated their intention to take the matter up with the legislatures in their respective states, so that specific authority may be given for aid to the work of this Committee.

It may be observed that the Committee does not differentiate in the service it is attempting to render, as between states which are contributors to its support and those which are not.

All funds of the Committee are expended only on warrants drawn by the Solicitor of the Committee, and approved by the Chairman; and a monthly audit of accounts is made. The financial records of the Committee are kept in duplicate, one set by the Chairman and the other by the Solicitor of the Committee, periodically balanced as against each other, and are at all times open to the inspection of any interested member of the Association. At the request of the Committee, the President of the Association designated Mr. E. E. Cone, statistician of the Corporation Commission of Virginia, to audit the accounts of the Committee and report to the Association. This audit has been made, and Mr. Cone's report will be submitted herewith.

Some states which desired to support the Committee's undertaking were unable to make a direct contribution of cash, but made arrangements whereby an employee of the Committee was taken on the Commission's payroll temporarily, or continuously at a small salary, and thereby the same result was achieved.

It may not be out of place to say that all expenses of the members of the state commissions serving the Committee by attendance upon hearings, etc., have been borne by their respective commissions, and have not been a charge upon any funds of the Association.

The foregoing outline, while brief, fairly covers the work of the Committee in carrying out its instructions from the Association. Acknowledgment should be made by the Committee of its appreciation of valued assistance rendered by Hon. A. E. Helm, Commerce Counsel of the Public Utilities Commission, State of Kansas, and by Mr. D. F. Jurgensen, Chief Engineer, Minnesota Railroad and Warehouse Commission.

Issues Presented in the Appraisal.

The foregoing statement of the Committee's work may be supplemented by a statement of the more important issues raised in the appraisal. There have been no rulings by the Interstate Commerce Commission itself upon any of the important issues raised in the appraisal. The work done by the Division of Valuation in organization, in the field, in pricing, in accounting and historical search, has covered a wide territory, and has necessarily taken time. Now that the work of the Division is completed as to certain railroads, the Commission will soon have to pass upon controverted questions which have arisen, and its determinations will control the future work of the Commission's forces unless reversed by the courts.

An Association of state railway commissioners recognizes at once the tremendous importance of the issues at stake. The creation of this Committee, with the broad powers given it, shows that the members of this Association are fully aware of the gravity of the the outcome of the valuation proceedings. The sums in dispute (laying aside values as to which no question could be raised) are the most huge which have ever been submitted to a civil tribunal for consideration: and even an admittedly low return on merely

the disputed items involves sums so great that finite human intellect can form no just concept of them. If the extreme propositions claimed by the carriers are adopted, or even a considerable portion of them, not only will it hereafter be impossible for any legislative body, state or federal, to prescribe any lower schedule of rates than at present in force, but the rate schedules now charged, fixed by the carriers themselves, will be found to be confiscatory of their own property. The future of regulation itself as a solution of the transportation problems is intimately connected with the outcome of the federal appraisal: if the contentions of the carriers are accepted, regulation through legislation or by legislative authority will fail to regulate, and the quicker the railroad properties are then taken over by the government, the cheaper they will be acquired and the inevitable be satisfied. To assist in the endeavor to avert such an outcome is the high duty and privilege of this Association.

Undue Haste in Appraisal to be Deprecated.

It is evident that as the results of the railway appraisal are momentous in their possibilities for good or evil, the first principle is that the work should be done so thoroughly that no question will remain open as to its accuracy and justness, or else that there should be no appraisal at all. If the appraisal is to be made under financial pressure or against a time limit, the government and the railways will not be on even terms, and the advantages which come from unlimited means, powerful organization, and years of experience, will all be with the carriers. If the federal government is to achieve the desired result, neither time nor money necessary to the end should be stinted. The enormity of the task before the Commission may be judged from the fact that its program, if carried out, means as an average, the appraisal of one operating railroad corporation with two hundred miles of line and terminals in addition, every working day for five years. If Congress should withhold the full amount of necessary appropriation to insure the utmost thoroughness in work, or in effect hold a stop watch upon the undertaking, so that the Commission and its forces would be consciously working under the stress of haste to avoid Congressional censure, the results of the appraisal can not be accepted by the country as satisfactory. Such a mistake in policy is to be deprecated.

Whether a Single Value to be Deduced a Question of Prime Importance.

The Committee regards of primary importance the question of construction of the Valuation Act, as to whether the Commission is directed, after investigating the three costs and the history of each carrier, to deduce a single sum and to state the same as being *the* value of the property of the railroad, without reference

to the purposes for which the appraisal was made, and without qualification of the term value. Such a construction of the Act has seemed to the Committee to be clearly negatived by its terms; and to be contrary to the intention of Congress as expressed in debates and antecedent history of the movement for a physical valuation, and, if adopted would lead to inconclusive, misleading, and confused results. Inasmuch as the decisions of the Supreme Court as to valuation are still largely unsettled, and the Valuation Act does not contemplate that some important elements which must be taken into account in determining value in a rate case shall be investigated in the present proceedings; and because of the loose sense in which the elusive term "value" is commonly applied to different and repugnant ideas, this Committee has consistently opposed a construction of the Act contended for by the carriers, which would culminate in a single ultimate finding of *the* value of the property of the carrier, based upon the principles which would be applied in a condemnation case.

In the tentative valuations so far served by the Commission are to be found no ultimate finding of value, in the sense contended for by the carriers, but there are findings of the various elements of value, stated separately and in detail as in the act required.

Original Cost to Date.

The Valuation Act requires the Commission to "ascertain and report in detail as to each piece of property owned or used" by the various common carriers for common carrier purposes, "the original cost to date."

Regardless of the individual opinions of the members of this Association as to the controlling effect of Original Cost to Date in the determination of value for rate purposes, it is indisputable that it is an element which Congress and the Supreme Court have ever placed first in the enumeration of matters which are to be taken into account as criteria of value, and that the mandate to the Commission to ascertain the fact stands unqualified. Findings made under the provisions of the Act are incomplete in so far as they fail to ascertain and report this element of value.

It is not denied that difficulties often attend the ascertainment of this important fact; and that frequently records are absent so that the attempt of the accountant to state the item from books of account is futile. Again, the words Original Cost have been used carelessly and in more than one sense. But within the meaning of the Valuation Act, Original Cost to Date can be ascertained and reported within close limits of accuracy in substantially every case; either from books of account or other reliable corporate records which have withstood the scrutiny of an audit by governmental authority, or by the cooperation of engineers and accountants, working backwards from the inventory of the present property to the prices applicable at the various times of construction, or by a combination of both methods. As an additional significant fact, a careful study and statement of the history and organization of the present and of any previous corporations operating the property, and the detail of the previous expenditures of money, and the purposes for which expended, required by the Act to be investigated and reported, will develop the sacrifice of the present investors.

The Division of Valuation has stated that in all cases where the records are available and are apparently reliable it will ascertain and state from such records the total cost to date; that it can ascertain and state the total cost of equipment and lands in substantially every case. But it has not interpreted the word "ascertain" in the Valuation Act as requiring an estimate of Original Cost where records of accounts are not to be had or are unreliable. The contentions of this Committee have to that extent been denied by the Division of Valuation, and it will be necessary to press the point before the Commission. It is of interest to note that the Division has stated that generally speaking it is at least as practicable to estimate original cost in the manner described as it is for the engineers to estimate the present cost of reproduction—if anything, within smaller limits of error—and that the Division expects in substantially every case to develop the history of the investment of the present owners.

The case of Original Cost to Date is illustrative of the policy the Committee is endeavoring to follow in the interest of the members of this Association. Manifestly the Valuation Act should receive such a practical construction as will make its results of the greatest possible utility. This Committee does not believe that the present proceedings necessarily or at all involve the question as to the relative weight to be assigned the item of Original Cost to Date. when ascertained, as compared with the other elements of value required by the Act to be found. But it is patent that the Act does require the item of Original Cost to Date to be ascertained and reported; that the situation is such that the facts can never hereafter be as well ascertained as now; that the Commission is given such latitude as to the sources of its information that this cost can in all cases be estimated even if the precise sum be not susceptible of demonstration; and that all courts and commissions regard Original Cost to Date as significant or even of greatest weight. Whatever the views of the Interstate Commerce Commission may be as to the weight to be attached to the finding in a determination of the ultimate value for rate purposes, these considerations justify insistence that every reasonable present effort be made to ascertain and report this cost figure in order that the findings will be of the greatest use to state commissions, both now and in the future.

Examination of the Act will show that the Commission is given discretion to determine the detail in which it will report the financial history of the carrier. This Committee has contended that the financial history is necessarily so interwoven with the item of original cost of intangible items for which value is claimed by the

carriers, that it is desirable that the income, profit and loss, and general balance sheet accounts should be stated in the report in the most full available detail, and at periodical intervals in order that there may be an intelligent and full examination of the claims of the carriers under the head of development costs, foreborne fair return, and with respect to the investment of the proceeds of donations, bonuses, surplus earnings, and replacement or depreciation funds. Every state commission which has had a capitalized-deficit or development-cost statement presented to it by a public utility will appreciate the importance of conserving this information when (as is the case) the government's accountants have unexampled opportunities to study the whole financial history of the carrier and its predecessors. There have been so few reports submitted for examination by the Accounting Section (and none since the Committee's request was presented) that the future policy of the Division of Valuation in this regard cannot be stated. From the experience of regulatory officers who have had to apply valuations to practical purposes, the failure to preserve this evidence when it was obtained or could be had, would be inexplicable.

Requirements of the Act as to Ascertainment of Land Values.

In addition to the general requirements of the Valuation Act as to the ascertainment of the three costs as to each piece of property owned or used by the common carrier for its purposes as a common carrier the following specific duty is cast upon the Commission:

> "Second. Such investigation and report shall state in detail and separately from improvements the original cost of all lands, rights of way, and terminals owned or used for the purposes of a common carrier, and ascertained as of the time of dedication to public use, and the present value of the same, and separately the original and present cost of condemnation and damages or of purchase in excess of such original cost or present value.
>
> Third. Such investigation and report shall show separately the property held for purposes other than those of a common carrier, and the original cost and present value of the same, together with an analysis of the methods of valuation employed."

A requirement as to the ascertainment and reporting of pertinent facts with respect to aids, gifts, grants, and donations, will be discussed later herein.

Reproduction Costs of Lands.

The Act in terms requires the present cost of condemnation and damages or of purchase in excess of present value to be ascertained and stated—a requirement which the subsequent decision in the Minnesota Rate Cases demonstrated was incapable of a rational answer. The position taken by the Division of Valuation (which is followed in the tentative reports served by the Commission) is that even Congress cannot require performance of the impossible,

and therefore no speculation will be indulged in as to the condemnation or hold-up purchase costs, or damages. Here the Division finds itself in sharp conflict with the strongly urged claims of the carriers, who seem for the moment to have overlooked the Minnesota decision.

Original Cost of Lands.

It will be seen that the Act contemplates the ascertainment of the original cost of the operating and non-carrier lands, contrasted with the present value. Original cost is believed by the members of this Committee to be the strongly controlling factor in the ultimate determination as to the weight to be accorded land values in a rate case. Its views in this regard have been urged upon the Commission —views which perhaps more properly arise when determining the relative weight to be assigned different elements in a rate case than in the present proceedings. As to these contentions the Commission has expressed no opinion.

There are practical difficulties in many cases in determining the original cost of the present property, and contrasting it with present value. It is a laborious undertaking, which will require the expenditure of money to carry it through, and in some cases the requirement cannot be met at all. But as the disputed principles in land appraisals involve sums aggregating fully half the outstanding nominal capitalization of the entire railroad system of the nation, this Committee has urged that no obstacle not insuperable be permitted to prevent the most detailed and accurate statement of these important facts. The labor and expense involved are warranted by what is at stake. Nor are the difficulties real lions in the path.

Some of the items of overhead expense included in the original cost of lands are to be apportioned; some apportionments of original cost must be made when the consideration covers several tracts, or the tract conveyed has been divided for classification or other purposes, and evidence de hors the corporation's records may be necessay to supply the answer. It is not an answer to say that apportionments are necessary; modern accountancy and jurisprudence do not regard the difficulty of the apportionment of values as an excuse for failing to find the basis for a reasonable division of property when necessary for rate purposes (vide Minnesota Rate Cases). More difficult problems than this must be solved before the appraisal is done.

Methods Pursued by the Division in Determining Present Value of Lands.

The methods pursued by the Division of Valuation in determining the present value of lands used for the purposes of a common carrier are well set out in the report upon the Norfolk Southern; which may be taken as typical:

"1. The appraisers, by the use of maps and personal inspection, became acquainted with the country traversed by the railroad generally, and with the lands of the carrier and the adjoining and adjacent similar lands, and made a general study of real estate conditions in the territory.

"2. An examination and study in detail was made of the carrier's lands and the adjoining and adjacent similar lands, and the non-carrier lands noted.

"3. A copy of the non-carrier list was submitted to the carrier for criticism, and the classification discussed with the carrier's representatives.

"4. Information from all available sources, official and private, including assessments, sales and opinions, was obtained.

"5. Zones of value were established and indicated on the maps.

"6. Final unit values of zones were determined. This value is the judgment of the appraisers, based upon investigation and consideration of all applicable elements of value.

"7 Areas of zones were ascertained by the computer and checked with original tracings, and are, in practically all instances, agreed upon with the carrier.

"8. The completed appraisal was checked and assembled, and rechecked.

"The following elements have been considered, and, wherever applicable, allowance made therefor: similarity, location, accessibility, utility, shape, size, corner influence, highway influence, grade, restrictions, physical conditions, transportation facilities, proximity to centres, character of soil, absorption, light, air and ventilation, and such other elements as suggested themselves at the time by the conditions peculiar to the particular location. Nothing has been added to the value of the railroad lands on account of special use as a continuous right of way, nor has anything been added or deducted because of the special use to which the carrier lands are now devoted.

"In ascertaining the value to be applied as a unit to the appraisers' zones of value, the fair market value of similar lands adjoining or adjacent to the carrier's lands was ascertained, and the unit of value of adjoining or adjacent similar lands constituted the values which were applied to the zones of the carrier's lands.

"Records of transfers, for the past few years, of similar adjoining and adjacent property were obtained. All available sales of land located within a reasonable distance were analyzed. Of these sales, those which reflected value in each zone have been reported on the field forms.

"The asking prices of adjacent or adjoining similar lands offered for sale were investigated and considered.

"In analyzing sales of property including improvements, the appraisers ascertained the value of the improvements and allowance was made therefor.

"Assessments of adjoining and adjacent similar lands were investigated and reported by the appraisers on the field forms, wherever found of value. The appraisers in analyzing assessments ascertained the general ratio of the assessments to the actual or market value of the land, and in arriving at their unit values were only influenced by the information gathered from assessments in proportion to their value as ascertained by analysis. These assessments varied, and the appraisers are of the opinion that in most instances the lack of uniformity and of the assessors' recognition of actual values in making assessments resulted in the assessments being of little aid, except in a few cases.

"Opinions were obtained from men whom the appraisers considered to be the best qualified by experience in buying and selling, or by knowledge of actual sales and by general knowledge of real estate conditions and values. In the instances where lands were valuable because of certain local conditions, or because of special adaptation to agricultural or other development, opinions were obtained from persons especially familiar with the natural and general use and development of the properties under consideration. Expressions of opinion from these men were obtained as to unit values per square foot, or per acre, or, where the values expressed covered entire lots or

farms, the appraisers either reported the value of such or reduced the same to units.

"The territory was divided into zones of value, and usually the zones were numbered consecutively for each county in a valuation section, beginning with No. 1. Street and highway crossings were zoned separately by the appraisers and these zones were given the same numbers as the zones crossed by the streets or highways, or the zones nearest the streets or highways. These highway zones are identified by the suffix "X".

"The same rule is applied to navigable waterways and streams, and the suffix "W" is used. The zones of land used for purposes other than those of a common carrier bear the same number as the adjoining or nearest carrier zone, followed by the letters "A", "B", "C", etc., according to the number of such parcels in each zone.

"The present market value per acre or square foot of adjoining or adjacent similar naked lands was ascertained and applied to the zones of the carrier's lands. As a general rule, city property is expressed in square foot units, and country right of way in per acre units. The units of value were determined by the appraisers and were placed upon the maps in each zone and recorded in the field forms."

It will be noticed that the present value of lands reported by the Land Section includes no allowances for expenditures for cost of acquisition, incidental or severance damages for the taking, or because the property is taken for railroad purposes and is a connected whole. No overhead expenses are built up on land values at any stage of the reproduction cost estimate. The original cost statements include such overheads, damages, etc., as were paid and are shown of record.

Land Classifications Employed.

The lands so valued are classified as follows:

Class 1—Lands Owned, and Used by Owner for its Purposes as a Common Carrier.

Class 2—Lands used by the Carrier, for its Purposes as Such, but Owned by some other party:
- Class 2-1—Owned or leased by other common carriers.
- Class 2-2—Owned by parties other than common carriers.

Class 3—Lands owned or leased by carrier, but used exclusively by another carrier, or other carriers, for common carrier purposes:
- Class 3-1—Lands owned.
- Class 3-2—Lands leased.

Class 4—Non-carrier lands owned, including value of improvements owned by carriers.

Lands acquired through aids, gifts, grants of right of way, or donations are included in the totals of each of the several classes above named; but the amount of such lands and the value thereof are separately stated. Excluded from each of the foregoing classes of property other than Class 2-2, are former streets, alleys and highways used exclusively by the carrier; streets, alleys, and highways used jointly by the carrier and the public; and certain bodies

of water crossed, and certain railroad crossings. These items are enumerated in the report.

Some sharp questions have arisen as to property classified as used for purposes other than those of a carrier. as certain roads have made sweeping claims that none of their lands were held for purposes other than those of a common carrier. Again, questions have arisen as to the inclusion of property used jointly. Certain carriers have urged that each joint user shall receive the full benefit of its occupancy—a proposal which involves an unwarrantable duplication of values. Other carriers have made claims for the inclusion of the values of the area in public highways longitudinally occupied by them, or allowances for the value of such rights.

If it be assumed that the present value of adjacent similar land is the present value contemplated by the Act to be ascertained and reported. the Committee has no fault to find with the general plan pursued by the Division. It is realized that after all, nothing is more uncertain than opinion evidence as to land values; that everything depends upon the industry, competency, and honesty of the individual land appraiser. Suggestions have been made by carriers that no figures be arrived at by the field appraisers until hearings have been had, or that the Division of Valuation abdicate its statutory function and arbitrate the land values with the carriers. Naturally the Committee opposed both suggestions. The state commissions can be of the utmost service in connection with this very uncertain question of land values, because of their familarity with local conditions, their general knowledge of the subject, and their superior facilities for obtaining the facts as to the values of similar lands located in their own jurisdictions. Even the commissions which have no engineering staff and those which have done no appraisal work can co-operate with the Interstate Commission and render valuable service in this particular.

While the carriers have not accepted the basis of the Division of Valuation, and the claims of the carrier made after checking the praisals by following substantially the same methods, and state results which differ so widely from those found by the Division that they are startling. For instance: In the case of the Norfolk Southern, the results announced by the Land Section of the Division of Valuation, and the claims of the carrier, made after checking the government's experts' figures, may thus be contrasted:

	Commission's Land Section's figures		Carrier's Claims	
	Acres	Present value	Acres	Present value
Class 1	9280.172	$1,990,844.28	10,100.687	$4,111,309.84
Class 2	2338.943	588,899.93	2,456.753	1,388 442 02
Class 4	2264.442	440,970,66	2,775.445	572,525 42
Total acres	13883.357		15,332.885	
Total value		$3,020,714.87		$6,072,277.28

This discrepancy is typical. In the case of Kansas City Southern, the carrier claims to have followed the precise methods employed by the Division of Valuation, and very largely to have gone to the same sources of information, and has built up a claim for present value of lands approximately three times that reported by the Land Section of the Division.

It requires little reflection to show the importance of a proper determination of this value. One railroad president is quoted as saying that on his system a difference of one cent a yard on the unit price of grading means fifty million dollars. Enormous as are the sums involved in differences of opinion as to unit prices on the physical elements of the railroad system other than land, when the differences as to land values of the charater stated are projected over the whole country, contests as to a few cents on a unit price of ties or grading becomes merely the haggling over a pickayune.

The function of the state commissions is plain. The figures placed on land values by the Division of Valuation are, wholly or partly, either too high, too low, or neither too high nor too low. The state commissions can with reasonable readiness determine which is the case. If too low, the carriers may be depended upon to develop the fact. If too high, the state commissions should show that they are excessive. If correct, the state commissions should lend their support to the figures of the Division of Valuation as against any extreme claims of the carriers.

Difficult questions are certain to arise, important in their effect, which have not been indicated in the above statement. The valuation of land when no other similar land exists in the neighborhood, the appraisal of filled or overflowed lands, accretions, riparian and water rights, subsurface easements, mineral rghts, suggest interesting prob!ems the solutions of which are still indefinite.

Aids, Gifts, Grants of Right of Way, and Donations.

Among the facts which the Commission must ascertain and report and which the states believe to be of great importance, are the amount and value of any aid, gift, grant of right of way, or donation made to any common carrier or to any previous corporation operating its property, by the United States or by any state, county, or municipal government, or by individuals, associations, or corporations. Similarly the Commission is required to ascertain and report the grants of land by the United States, or by any state, county, or municipal government, the sum derived from the sale of any portion, and the value of the unsold portion when acquired and now. If any concession of allowance was made to the United States, or to any state, county, or municipal government in consideration of such aid, gift, grant or donation, the amount and value thereof is to be reported.

By Valuation Order No. 16, entered March 15, 1915, the Commission requires common carriers, whose property is being valued,

to report the details of such aids, gifts, grants and donations. Parenthetically, the returns of this schedule have generally not been disconcertingly full or prompt.

The Division of Valuation has twice asked the state commissions as to what assistance they can give in securing the data as to aids, gifts, grants, etc., called for by the Valuation Act; and for suggestions for independent inquiries by the Valuation Division. It is apparent that the local authorities are in a position to see that the federal commission receives the full information which is necessary to permit it to make the return required by the Act of Congress. In fact, the state commissions in this regard would seem to be more advantageously situated than the federal government. Several commissions already have this data in their files; others can secure it by a search through state or local archives, or at least can put the Division of Valuation in touch with the proper local officers from whom the full and acurate information can be obtained.

It is a matter of common understanding among state commissions that in many cases, and almost universally in certain sections, the value of the aids, gifts, grants and donations equalled or exceeded the cost of the earlier constructed railroads. The importance of a full return as to these items is attested by the insistence with which the state commissions have always urged that they should be investigated and reported.

The difficulties which exist in many cases in determining the value of these aids, gifts, grants, and donations as of the time of acquisition is recognized by the Committee. It is easier to determine now the present value with fair accuracy than the value twenty to fifty years ago. On the other hand, the margin of possible error in estimation is smaller when the values were inconsiderable. The importance of the item as one of practical utility in a valuation for rate purposes warrants a demand that nothing short of an unsurmountable abstacle be permitted to block the Commission from making the findings in this regard which Congress has directed. Evidence of that character and degree of finality which we would prefer is not always to be had; but when evidence of such character is absent, the best evidence of which the case in its nature is susceptible must suffice, and ordinarily does permit the mind to find a fact to a moral certainty in matters of even the gravest concern

Ascertainment of Reproduction Cost New.

The methods pursued by the Division of Valuation in the estimation of the cost of reproduction new of the various properties owned and used for common carrier purposes are in the main the same which have been employed by various state commissions, and present no points of difference which call for extended comment. As a preliminary, the carrier is required to furnish the Commission with complete maps and schedules of its real property, equipment, machinery and the like. Then a survey is made by the government engineers, generally in company with a pilot or representative of the carrier. Copies of the field notes are furnished the carrier and a time fixed for the objection on account of errors. In the case of certain large terminal properties the process is reversed, and the carrier's forces make the survey, in company with representatives of the Commission, and furnish the goverment's party with copies of the notes. From the field notes so prepared computations of quantities are prepared, and checked by the carrier at the time. The application of prices to the units thus computed is done by the government's engineers at the District office, independently from the carrier.

The Inventory.

Until the present time the differences between the carriers and the government as to unit quantities have been within the allowable limits of error. However, no state commission has yet completed a detailed verification of quantities, and this desirable check is absent. Certain of the state commissions have undertaken to check the inventories within their jurisdictions in their entirety; other commissions are verifying particular valuation sections by making precise surveys; and others will give each inventory as careful a check as inspection of the line, examination of available office data, and a knowledge of construction conditions will permit, short of actual resurvey.

In connection with the ascertainment of quantities in the field, this Committee has urged, and now repeats its recommendation, that whenever possible, the state commissions accompany the field parties of the government with competent engineers in the employ of the state, to the end that there may be no eventual possible suspicion of inaccuracy in this fundamental part of the work, and that the results obtained may be accepted by the states as accurate enough for all their own purposes. This recommendation involves no thought of lack of confidence in the skill and integrity of the representatives of the government in the field; and the suggestion made has the hearty approval of the Commission itself, and of all the responsible officials of the Division of Valuation. If the federal appraisal is to be of the utmost benefit to the states, it must be so made that when completed the state commissions can say to their constituents that as far as the inventory was concerned, they know it is right, because they followed it as it was made and are satisfied as to its accuracy. A state commission which omits the opportunity to follow the field work of the government as it progresses will doubtless find it has the burden to bear if it afterwards complains of irregularities and inacuracies which timely observation and complaint would have corrected.

As the Committee has already advised the state commissions, opportunities for the states to observe the field work are already

provided. By memorandum No. 138, November 30, 1914, the Director notified his Engineering Board that the Commission had approved instructions that the state commissions might be permitted to have engineers accompany surveying parties, take copies of the field work, etc., as the work progresses, provided it did not embarrass or add to the expense of the government's work. Memorandum No. 149 directs the various Engineering Sections to notify the state commissions whenever work is begun upon a railroad in that state: and that the state commissions shall have whatever reasonable access to the work, both in the field and in the office, can be given without impeding the work itself.

In order that results obtained by the federal government's and the state's engineers may be comparable, the instructions laid down by the Commission for the guidance of its field forces should be kept in mind. Copies of these have been transmitted by the Commission to the state commissions.

There are differences between the practices of the government's forces and the claims of the carriers in certain respects as to unit quantities which, while enormous in the aggregate, are overshadowed in the importance of their results by other contested issues. The cumulation of aggregated items of this description, however, with the addition of overheads which accompany them, and overheads built upon overheads, reaches a staggering height, and it is necessary their propriety be demonstrated. Reference is made to hidden quantities, allowances for subsidence, for shrinkage in grading and ballast (all of which have been generally agreed upon between the carrier and the government), to claims for adaptation and solidification resulting from the lapse of time and forces of nature, bank protection due to natural vegetation, and to claims for contingencies and inventory omissions, which have so far received little favorable consideration from the Division of Valuation.

Construction Program.

In early conferences between the Commission's officers, representatives of the carriers and of the states, the suggestion was thrown out by the railroads that the government and the carriers agree in each case upon a program to be assumed as a basis for the hypothetical reconstruction of the property. This suggestion was opposed by the states. The government forces have used their own discretion in mapping out a program assumed for the purpose of determining their reconstruction conditions, and in every instance so far the carriers have found fault with the assumption. The program assumed is of importance with respect to the items of interest and taxes during construction. It is a factor in the determination of the material, labor and transportation costs, and bears upon the estimate of a balance of earnings and expenses from operation during construction. It has been the announced intention of the Division of Valuation to assume the shortest period

which is consistent with economical construction, which ordinarily is short enough that any credit balance from operation during the construction period will be absent or negligible.

Because of their knowledge of local conditions and construction practices and facilities, the engineering forces of the state commissions should be peculiarly well qualified to test the tenability of the assumptions made by the Commission as to a reconstruction program. Such construction history as is available—both with respect to the particular carrier and other lines—should be studied and the results be made accessible to the government forces.

Unit Prices.

The unit prices applied to the inventory quantities by the Engeering Section of the Division of Valuation have been assailed violently all along the line by the carriers. On the other part, certain state commissions interested in appraisals submitted for examination have taken excepton to some unit prices as being manifestly excessive. Various claims for extras, etc., are in dispute. Some items, such as assessments for public improvements, have been disallowed *in toto* by the Commissioner's engineer, while contended for by the carriers.

Apparently the Commission has spared no pains to secure adequate information upon which to base its unit prices. By a series of orders it has directed the carriers to file with it returns showing important purchases, construction, etc., in detail which will permit proper analysis. A list of these valuation orders and of the schedules called for is set out in an appendix to this report The returns to this series of orders are kept under the direction of the Division's Central Cost Bureau, at its general offices in Washington. A huge amount of other cost information has been collated from construction records, manufacturers' catalogues and discount sheets. The Central Cost Bureau is constantly making exhaustive studies for the general assistance of the District forces. Each District collates, independently of the Central Cost Bureau, cost information from the records of railroads under examination and others located in the same territory. In some cases the District engineers have made use of the cost data collected by the state commissions. The Accounting Section's work is coordinated with that of the Engineering Section in this regard. As might be expected, the facilities of the federal government for obtaining information of this character in a nation-wide survey are unexampled, and have been taken advantage of.

The independence of the Engineering Districts in determining prices has resulted in widely divergent methods of stating inventory quantities and unit prices, and inconsistencies and incongruities have appeared, when the work of one District is checked as against another. The desirability of a standardization of methods of stating the quantities and applying unit prices is ap-

parent to this Committee, at least, and doubtless standardization will grow with the progress of the work.

This valuable information ought to be, and doubtless can be, made of assistance to the interested states, not only in connection with appraisals of railroad properties, but in connection with the appraisal of public utility properties generally. The catalogue of articles which enter into the railroad systems of the country, and as to which information has been gathered and collated by the Division, is so comprehensive that scarcely any article used by a public utility of whatsoever description is omitted. One of the functions of this Committee is to assist members of this Association to take advantage of opportunities of this character, so far as the Division of Valuation may find it consistent with the public interest and the means of the Committee enable it to honor specific requests for such service.

A number of state commissions have either requested or directed the carriers (telegraph and telephone companies included) within their jurisdictions to file with them copies of all maps, profiles and schedules filed wth the Interstate Commerce Commission pursuant to the various valuation orders of that body. Such state commissions have thereby acquired a large amount of live and useful cost data at an expenditure of time and money, kept at a minimum both for the carriers and the commissioners.

The unit price embraces three elements: material, labor and transportation. In the opinion of the Committee, all concerned have taken for granted in the past with respect to the transportation factor in unit costs; and further study is indicated before past assumptions should be perpetuated in the findings presently to be made. The Committee has this subject under consideraton for the purpose of submitting its views as to such a study at the proper time.

Engineering.

The practice of the members of the Engineering Board in the various districts has differed as to the estimation of engineering as a part of the reproduction cost estimate. A uniform method of statement has been adopted whereby the estimate is stated in a percentage of the various Road Accounts, excluding Engineering itself, Land, Assessments for Public Improvements, Revenues and Operating Expenses during Construction, Cost of Road Purchased, Reconstruction of Road Purchased, and Unapplied Construction Material and Supplies. No engineering has been estimated on equipment accounts, other than may be carried in the unit price applied.

The carriers have made a general claim that the minimum engineering estimate should be 5% of the accounts named, and in no case less than $750 per mile. Certain railroads have broadened the claim by asking that land shall be included in the Road Accounts on which the percentage is based.

The state commissions should be in position to supply considerable valuable information upon this item, often in respect to the particular road under investigation, and generally as to other roads of similar character and construction characteristics in the same territory.

While the carriers are making the claims which have been noted, a number of the state commissions are prepared to controvert any allowance for engineering for purposes of reconnaisance and location; because the hypothesis of the obliteration of the present rail line, while leaving the adjacent geographical conditions intact, automatically amounts to a line location, so that no preliminary reconnaisance or location survey will be necessary. The claim of the carriers for an allowance of 5% at least, with a minimum of $750 per mile, is evidently excessive in many cases; and should receive the careful attention of state commissions in territory where construction is reasonably light

General Expenditures.

As might be expected, there are some sharp differences between the claims of the carriers and the allowances made by the Engineering Section of the Division of Valuation. The large difference in Interest, and in Taxes during Construction growing out of the varying construction programs assumed have already been mentioned. On the other hand, certain items, such as Taxes during Construction, and Organization Expenses, are regarded by the Committee as very questionable in the shape in which they have been included in the reports so far submitted for examination. The proposal to base overhead expenditures upon land values, as well as upon the other road acounts and equipment expenditures, will be opposed as negatived by the decision in the Minnesota Rate Cases.

Deduction of Depreciation From Reproduction Cost.

Although the ascertainment of the cost of reproduction less depreciation is required by the plain terms of the Valuation Amendment, the carriers have at all times contended that as long as the property is maintained out of operating expenses at a standard which permits it to give unimpaired service, no depreciation exists which can be taken into account as a deduction from reproduction cost. The Committee has taken the position that the words "cost of reproduction less depreciation" were deliberately employed in the Act by Congress in the accepted meaning and signification recognized at the time by courts and commissions, and that they require a consideration of the units of the property separately, and not merely as a combined whole.

The Engineering Board of the Division of Valuation has stated the principles it believes to be applicable in its memorandum to

the Director, No. 226. A copy of this memorandum has been furnished by the Committee to each state commission, and the principles involved and detailed instructions for their application need not be repeated. The state commissions find themselves generally in substantial accord with the principles set out in the Memorandum; but reserve the right to suggest deviations in detailed application when the facts in particular cases require such course in the interest of accuracy.

Neither the states nor the carriers should have any real motive for unduly lengthening or shortening the lives of structures used as a basis for the depreciation computations. If too long a life is taken, the cost of reproduction less depreciation is increased, and if a return is based thereon, the return is increased over what it would be if a shorter life were taken and the cost of reproduction less depreciation was thereby made a smaller sum. On the other hand, the longer the life, the smaller the credit permitted as an operating charge for a replacement or depreciation annuity, and vice versa. A long life will mean a high reproduction cost less depreciation, a higher permissable rate of return, and a lesser amount which the carrier must lay aside before having a surplus out of which dividends can be met. The importance of a proper balance in the determination calls for the exercise of a sound judgment based upon an exhaustive study of the facts—a study which the federal government has apparently foreseen is necessary and has therefore made.

Other Values, and Elements of Value.

Thus far the report has had to do with costs which inhere in physical property. The Valuation Amendment, evidencing the desire of Congress that all of the facts which under any theory may be pertinent shall be assembled and perpetuated, requires the Commission to

> "Ascertain and report separately other values, and elements of value, if any, of the property of such common carrier, and an analysis of the methods of valuation employed and of the reasons for any differences between any such values, and each of the foregoing cost values."

Up to the present time the railroads appraised have been among the weaker lines, as to which it would tax the ingenuity to find any other value or element of value than those inhering in the physical property, and as to those lines the tentative valuations served by the Commission report that no evidence has been submitted as to any such values. These tentative valuations have not progressed to the stage where the parties have been heard formally, and therefore the issues are still indefinite.

The carriers have made a general claim that the appraisal is to be made along the same principles as if the property were being condemned, and therefore other values attach, either to specific

pieces of property or units or parts of the property, or to the property as a whole. These latter values are defined by them substantially as follows:

Value of unity of use and connected operation: in that the separate articles of physical property constituting the railroad are joined together in a unity of use.

Going concern value: because the plant is in operation and has an established business in active and successful operation earning revenue.

Location value—traffic: representing the earning capacity of the property due to its favorable location with reference to command of traffic, including the existence of all the traffic producing industries located along the line of the carrier, the advantages of the railroad of connections with other carriers, the potential traffic in its tributary territory and all other features bearing upon its present and prospective traffic earning capacity.

Location value — operation: resulting from economy of operation due to gradient, alignment and other physical characteristics, climatic conditions, adequacy of terminals, equipment and other facilities, fuel supply, efficiency of operative organization, and all other features bearing upon the cost of operation and maintenance.

Franchise value: the right to exist and to operate

Many other factors are suggested as undoubtedly contributing to the productiveness of the use of the property of a railroad, and which in due course the Commission will be asked to measure.

One of the railroads under examination has supplied the details which permit us to see where a lively imagination will lead, starting from the premises furnished by the carriers' committee. Including discounts on securities, the original cost of the railroad in question was stated by it as between fifty-five and fifty-six million dollars. Its "other values and elements of value" claimed, over and above physical property, are almost exactly twice the original cost of the physical properties and the discounts, or approximately $110,000,000. Included in the claim as economic costs or other values are such items as the expenses of prior receiverships and reorganization, the cost of securing co-operation of the security holders antecedent to reorganization, the cost of abandoned property long since written off out of the earnings or as against surplus; the capitalized savings in expense because the road has facilities and traffic arrangements for the interchange of cars with connecting lines, and is not obliged to break bulk and transfer from car to car either at its terminals or at state lines. The usual development costs are brought up, based on shortage of a hypothetical fair return on these values, with compound interest on such short ages. This return and compound interest are also claimed as an element of value upon donations made by the public, upon betterments to the roadbed resulting from natural causes, and upon the increment in the value of physical property which is due to advancing prices of labor and materials over actual cost.

Procedure Under the Act.

At the date of this report tentative valuations have been served by the Commission in a few cases having to do with small roads or systems. The issues have not been made up by the filing of protests, and no hearings have been had before the Commission.

The Valuation Amendment does not require that the tentative valuations shall be served upon the state commissions; but at the request of this Committee the Interestate Commerce Commission has provided that tentative valuations will be served upon the state Commissions as well as the respective Governors in the affected territory, and that a copy will be delivered to the Solicitor for this Committee. No rules of procedure have been adopted by the Commission at the present time. It has been ruled in these initial cases that the thirty days for the filing of protests will begin to run from a future date named, which normally will be after service is completed. Time is short, and prompt action is necessary after the state commissions receive copies of the tentative reports if objectionable features are to be discovered and protests filed in due form and within the time limited.

The form in which the first tentative valuations appear has been made clear to each state commission by the Committee. It is important that as far as possible the tentative valuations shall be cast into such form that their findings will be self-contained, and may be used as a starting point for future continuations or supplementary appraisals, for the computation of depreciation annuities, apportionments of value, and the like.

No definite information is at hand as to the course of procedure to be followed upon the hearing of protests against the tentative valuations. When this information can be had in authentic form it will be supplied to the state commissions.

Conclusion.

It has not been the purpose of the Committee to foreclose the liberty of action of any state commissioner or commission in these valuation proceedings. Rather has the Committee attempted to safeguard public interests which have substantially unanimous support as settled policies, and to shape the appraisal as an administrative matter so that whatever results are reached by the federal authority may be upon principles which can be approved and expressed in a form useful to the states in dealing with their local problems as well as their interstate rights.

This Committee's work at the best can only supplement that of the state commissions, each of which must bear its full share of the responsibility, and upon which must come the major burden of safeguarding the interests of the citizens of the respective states before the federal Commission. What this Committee can do is in furtherance of the work of the individual state commissions, and cannot be a substitute therefor. This Committee's service can be and should be extended more than its present means have permitted.

Enough has been said to show the gravity of the situation. The stakes at issue are beyond human comprehension. Responsible officers of one railroad (now in the hands of a receiver) have stated that the results of the appraisal will justify a valuation of its stock double its par amount and about five times its present market value. The functions of the state commissions in the emergency are obvious.

The Committee respectfully submits this report of its progress for the approval of the Association.

October 21, 1916.

Charles E. Elmquist, *Chairman*,
Joseph L. Bristow,
George A. Henshaw,
Edward C. Niles,
Walter A. Shaw,
Max Thelen,
Clyde B. Aitchison,

Committee.

APPENDIX.

REFERENCES TO IMPORTANT VALUATION ORDERS OF THE INTERSTATE COMMERCE COMMISSION, REQUIRING INFORMATION FROM COMMON CARRIERS.

Valuation Order 1 (the so-called "Map Order"), modified and supplemented by Valuation Orders 5 and 6. Provides specifications for maps and profiles of railroad lines, which govern maps and profiles filed with the Commission.

Valuation Order 2, as modified by Order 10. Requires the filing of schedules of abandoned property, showing original cost, date of abandonment, and disposition and present status of the property.

Valuation Order 3. Providing that records shall be kept and reports shall be made to the Commission as to all extensions, improvements or other changes in the physical property of every common carrier after June 30, 1914, classified by states, and showing in detail units and quantities of material and labor.

Valuation Order 4. Requires an annual inventory of material and supplies to be made and kept.

Valuation Order 7. Requires the filing of schedules of land, showing original cost, and classifying as held for carrier purposes or purposes other than those of a common carrier.

Valuation Order 8. Requiring the recording and reporting of a register of equipment (rolling and floating, work, and shop and other machinery), showing original cost to date.

Valuation Order 11. Requires the filing of inventories of corporate records, documents and papers, showing location and custodian.

Valuation Order 12. Schedules of industry tracks to be filed.

Valuation Order 13. Requires the making and filing of schedules and inventories of quantities, units, and classes or kinds of property in roadway or track, bridges, buildings and all other structures, signals, interlockers, telegraph and telephone lines, electrical apparatus, and any and all fixed physical property except lands and equipment, which are covered by Valuation Orders 7 and 8. *supra.*

Valuation Order 14. Schedules to be filed showing important purchases made and net prices paid by steam railroads for material of a large number of enumerated classes, and also rates of compensation for labor.

Valuation Order 15. Requires schedules pertaining to privileges given and leases made by steam railroads.

Valuation Order 16. Requires schedules of all aids, gifts, grants and donations, and other data called for in paragraph of Valuation Act marked "fifth."

Valuation Order 17. Schedules required for telegraph companies showing important purchases made and net prices paid for material of a large number of classes of property, also rates of compensation paid for labor.

Valuation Order 18. Similar in scope to Valuation Order 17, applicable to Class A and B telephone companies.

Valuation Order 19. Requires schedules to be filed by steam railroads showing important purchases of material, net prices paid, and rates of compensation for labor, pertaining to telegraph and telephone property.

Valuation Order 20. Requires statements showing the corporate history of the common carrier appraised and its predecessors, and the chain of title.

MSH 21394

END OF
TITLE